

December 8, 2003

Honorable Mayor and Members
of the City Council
City of Romulus
11111 Wayne Road
Romulus, MI 48174

Dear Mayor and City Council Members:

We recently completed the audit of the financial statements of the City of Romulus, Michigan for the year ended June 30, 2003. During the year, the City experienced several significant changes with the adoption of Governmental Accounting Standards Board Statement Number 34 and the implementation of a new financial management software system. These activities required an extraordinary amount of effort from the City's Finance Department in particular and other City personnel and departments.

Government Accounting Standards Board Statement 34

As previously communicated to you, Governmental Accounting Standards Board (GASB) Statement 34 is now here! You will notice a very different look to the financial statements. As we mentioned earlier, preparing for this new reporting model has been a long and arduous process for the City's accounting department.

Although there are many differences with this new reporting model, the major additions are as follows:

- Management Discussion and Analysis: Management is now required to give an overview of the City's overall financial position and results of operations.
- Government-wide Financial Statements: These additional statements adjust the normal fund-based statements into a combined, full-accrual format. This allows a financial statement reader to see the City from a longer term perspective (i.e. are today's taxpayers paying for today's services?). These statements show capital and infrastructure assets, as well as long term debt as part of the City's financial picture.
- Budget Comparison: A financial statement reader will now be able to view not only the actual revenue and expenditures of the City as compared to the current budget, but also as compared to the original budget.

The GASB believes this new model will provide a more complete picture of the financial position of the City. We would be happy to schedule a time to provide a more detailed overview of this new reporting model so that you can obtain the greatest benefit from it.

Government Accounting Standards Board Statement 34 (continued)

It is important to note that, although the implementation process has received the most attention, there are on-going aspects of GASB 34 that will continue for future years. With additional statements, reconciliation from fund-based to Government-wide reporting, infrastructure tracking and more being added by this new reporting model, there is more preparation needed for the annual financial reporting process.

Cash and Investments

In planning and performing our audit, we considered the City's internal control structure in order to determine our auditing procedures for the purpose of expressing our opinion on the general purpose financial statements. The consideration we gave to the internal control structure was not sufficient for us to provide any form of assurance on it. However, we noted certain matters involving the internal control structure and its operation that we consider to be reportable conditions under standards established by the American Institute of Certified Public Accountants. Reportable conditions are significant deficiencies in the design or operation of the internal control structure that have come to our attention and, in our judgment, could adversely affect the City's ability to record, process, summarize, and report financial data consistent with management's assertions inherent in the financial statements.

A material weakness is a reportable condition in which the design or operation of one or more of the internal control components do not reduce to a relatively low level the risk that errors or irregularities in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of internal control would not necessarily disclose all matters in internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses as defined above. The following item is considered to be a reportable condition and a material weakness. The remainder of the letter contains other items for your consideration.

As part of the implementation of the new financial management system, a pooled cash program was newly established which allows the City to report all cash accounts in one agency fund in an effort to provide better cash management and transfers between funds. The new accounting system and the pooled cash program were activated in January 2003. Along with the efficiencies and improvements in the new system, the implementation of the pooled cash program required City clerical staff to learn and develop a new reconciliation process which affected the timeliness of the bank reconciliations. As a result, bank reconciliations for the period January 1, 2003 through June 30, 2003, were not prepared timely as in the past. Additionally, we noted during the audit that cash receipt batches were not posted timely to the general ledger system which would have complicated the reconciliation process.

The Treasurer's office is responsible for the investment of the City's surplus monies. The Finance Department works with the Treasurer's Office to record investment transactions in the City's general ledger. For the year ended June 30, 2003, investment activity for the period from January 2003 through June 2003 was reconciled until after year end. As with the City's bank reconciliations, we recommend that investment transactions be recorded in the general ledger on a monthly basis. We suggest that the Treasurer's office and the Finance Department review this process, including the information to be provided by the Treasurer's office on a monthly basis.

Long-Term Planning

The year ended June 30, 2003 resulted in a small decrease in General Fund fund balance of approximately \$93,000. This occurred as a result of declining state shared revenue and the precarious status of Airport Parking Fees which were both directly impacted by the Michigan Legislature. The City was able to avoid a larger reduction to General Fund fund balance due to the tax rebate received from the closing of two tax increment financing districts.

However, the financial future for all Michigan local units of government (not just Romulus) remains challenging and uncertain. As we have discussed in the past, property tax revenue growth on existing property is limited substantially by both the Headlee Amendment and Proposal A. As you recall, the Proposal A inflation factor for 2003 property taxes is 1.5 percent. The difficulties with state shared revenue, another significant General Fund revenue source, are expected to continue. At the same time, the demand for public services continues to increase.

In light of recent developments, new revenue sources may exist that will improve the City's financial condition. Until that time, we would encourage the City to carefully review its budget over the next several years to ensure that sufficient revenue exists to finance the City's operations. To assist with this process, City may want to develop a five-year financial model to provide the City with another tool to assist in long-term decision making. The City could also extend this process to its water and sewer fund as well. The City continues to be in receipt of monies from past years related to the construction activity of the downriver sewage disposal system that will need to be considered before the project is ultimately paid for.

Cash Receipt Activity

During the year, the Building Department changed locations and began to accept payment for permits issued. During our audit, we gained an understanding of the cash management procedures used by the Building Department and offer the following comments and recommendations:

- Occasionally, building permits are issued to customers before payment is received. The clerk issuing the permit makes a notation in the computer system that the permit is inactive due to non-payment. Once the customer has made the payment, the clerk must remember to remove the non-paid status from the customers account. To ensure that payment is received for all permits issued, the Building Department should consider not allowing customers to receive a permit unless payment is received.
- The computer system used to track permits does not have the capability of printing in one report a listing of all permits issued for a given day. As part of this new process, the Building Department should review alternatives available to produce this listing to support monies collected for deposit.

During the audit, we noted that the City seized gambling proceeds of \$316,535 as part of law enforcement activities during the year. These funds were remitted to the Treasurer's office for deposit. We were not able to review documentation supporting the receipt of these funds. The facts associated with these activities are not typically consistent, but, nonetheless, we encourage that a procedure be followed to maintain documentation with the cash receipt for these events.

Transition Issues

Now that the City has progressed through the implementation of the new financial management system and the adoption of GASB 34, we encourage the City to review certain aspects of this year's annual financial reporting process as there was a considerable amount of detailed information that was developed that can be used to improve the accounting system going forward. In addition to cash and investments, areas such payroll processing, payroll posting, compensated absences and encumbrance rollover should be considered as part of this process. As the City completes its implementation of various modules of the new financial management system, the City should review its current system of recording delinquent personal property taxes and the coordination of a detail subsidiary ledger with the general ledger.

LEGISLATIVE ISSUES

Revenue Sharing

The City has and will continue to feel the effects of the slow down in the State's economy. State shared revenue accounts for approximately 19% of the City's total General Fund revenue. Because of slower than anticipated growth in the State's sales tax collections (the sole source of revenue sharing payments to local units of government) and the State's budget problems which have resulted in additional appropriation reductions to the revenue sharing line item in the State's budget, revenue sharing payments for the State's fiscal years ending September 30, 2002 and 2003 were less than originally projected.

The previous Governor's original budget recommendation for fiscal year 2002/2003 was to keep total revenue sharing payments to cities, villages, townships, and counties constant (or frozen) at the fiscal year 2001/2002 level. This recommendation included a reduction of approximately \$112 million from what the statutory formula would have otherwise allowed. As was well publicized, following the introduction of the previous Governor's fiscal year 2002/2003 budget there was an attempt in July 2002 to veto all statutory revenue sharing from the State's 2002-2003 budget. The attempt was not successful and the veto was overridden by the Michigan Legislature. However, in December 2002, revenue sharing was cut another \$53 million by an Executive Order of the previous Governor.

The budget proposed and approved for the State's 2003/2004 fiscal year included another reduction to state shared revenue of 3% from fiscal year 2002/2003 levels. As you aware, the State's budget woes continue. In October 2003, the State's consensus revenue estimating conference revealed that the State faced another over \$900 million shortfall in its current 2003/2004 fiscal year. In December 2003, the Governor issued an Executive Order reducing revenue sharing by another 5 percent. As a result, we continue to urge the City to be conservative in its estimation of state shared revenue as this line item in the State's budget remains vulnerable.

We have attached a chart to provide you with more detail on what has occurred with revenue sharing relative to the City of Romulus. The chart demonstrates the impact that these cuts in revenue sharing by the State have had on the City of Romulus. We will continue to update the City as developments occur.

Retiree Health Care Funding

The Governmental Accounting Standards Board recently issued an exposure draft addressing the accounting for retiree health care. As you know, the promise to provide health care to retirees is very similar to the promise to provide an annual pension check. As a result, GASB is proposing changes that would result in the City having to have an actuarial valuation to define the liability and the liability would need to be disclosed in the financial statements. In addition, the City's funding status, or the progress it has made in accumulating assets to pay for this liability, would also be disclosed. Lastly, the City would be required to make an annual contribution equal to the amount that the actuary deems necessary to fund the liability over a 30 year period. As you know, the City of Romulus has been setting funds aside for this liability. The City has approximately \$1,730,000 in the Retirees' Insurance Benefits Fund. While this is a good start toward funding, the City should consider having an actuary evaluate the funding progress the City has made and how the City's current annual contribution would compare to the contribution required if the benefit was actuarially funded.

New Homestead Audit Program

Public Act. 105 of 2003 provides new authority for local units of government and the Michigan Department of Treasury to share homestead information to determine if a resident is illegally claiming an homestead exemption on property. As you recall, following the passage of Proposal A in 1994, individuals in Michigan are allowed only one homestead for property tax purposes. A residence which is not an individual's homestead pays property tax at the non-homestead rate. The Michigan Department of Treasury will publish additional guidance related to this new law.

Land Use Council Report Released

The Michigan Land Use Leadership Council, a 26 member body created by an executive order of the current Governor, concluded their work in August 2003 and have issued a report to the Governor and the Michigan Legislature. The report contains over a hundred recommendations on growth and development matters in the State of Michigan. As part of the discussions leading up to the report issued by the Council, there was considerable discussion regarding targeting additional Federal and State monies to "commerce centers" (communities in highly populated counties providing infrastructure services). The discussions also included providing communities located in commerce centers receiving access to new and more powerful development tools. A copy of the final report is located at <http://www.michiganlanduse.org/finalreport.htm>. Recommendations included in the report will require legislative action.

ACH Arrangements

Recently, Public Act 738 was passed, which allows local units of government to make and accept electronic funds transfers (ACH payments), if the local unit adopts a formal policy. While local units of government may have already been using the ACH system for payroll tax remittances and for the direct deposit of payroll, this new law requires a policy to be adopted. We can provide the City and its legal counsel with additional information to comply with this Act.

Municipal Finance Act Revisions – Reminder

The Municipal Finance Act was amended during 2001. Beginning after March 2002, communities are now required to submit a filing once a year with the Michigan Department of Treasury. The old ten day "exemption from prior approval" process has been eliminated and is replaced with this qualification process. This filing will serve as a pre-approval for future debt issues. The current filing is due within six months of the City's year end (June 30, 2003) and is good for one year thereafter. The Michigan Department of Treasury has also indicated that a separate qualifying statement may be required for each component unit of the City (i.e. a separate qualifying statement for the Downtown Development Authority, etc.).

We would like to express our thanks and appreciation for the courtesy and cooperation extended to us by the City staff during the audit. We appreciate the opportunity to present these recommendations for your consideration and will be pleased to discuss them further at your convenience.

Yours truly,

PLANTE & MORAN, PLLC

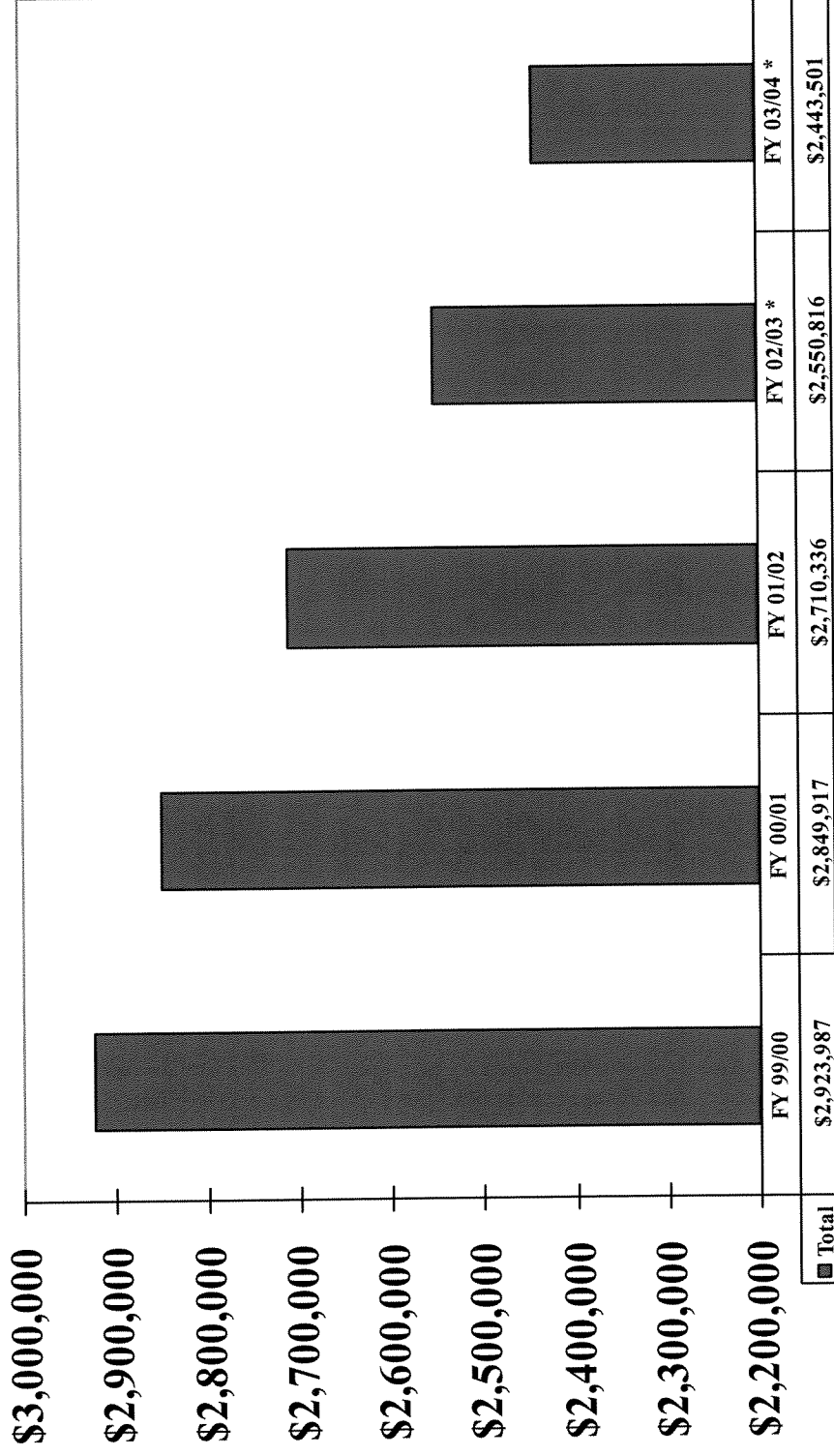


Frank Audia



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Total State Shared Revenue – City of Romulus



•Projected (Data Source for all State Fiscal Years Michigan Department of Treasury).